Calendar No. 207

100TH CONGRESS
1st Session

SENATE

REPORT
No. 100-88

AMENDING THE HART-SCOTT-RODINO ANTITRUST IMPROVEMENTS ACT OF 1976

JUNE 25, (legislative day JUNE 23), 1987.—Ordered to be printed

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Mr. BYRD (for Mr. BIDEN), from the Committee on the Judiciary, submitted the following

REPORT

together with

MINORITY VIEWS

[To accompany S. 431]

The Committee on the Judiciary, to which was referred the bill (S. 431) to amend the Hart-Scott-Rodino Antitrust Improvements Act of 1976, having considered the same, reports favorably thereon with an amendment and recommends that the bill as amended do pass.

CONTENTS

		Page
I.	Purpose of bill	1
II.	History of legislation	3
III.	Discussion	3
IV.	Text of S. 431 as amended	5
V.	Section-by-section analysis	5
VI.	Cost of legislation	6
VII.	Regulatory impact statement	7
VIII.	Changes in existing law	7
IX.	Vote of the Committee	8
X.	Minority Views	9

I. PURPOSE OF BILL

The Hart-Scott-Rodino Antitrust Improvements Act was enacted in 1976 to enhance enforcement of the antitrust laws. Section 201 of that Act added Section 7A to the Clayton Act, establishing a pre-merger notification system. Under that system, proposed mergers

S523-5

valued over specified monetary amounts must be reported to the U.S. Department of Justice and the Federal Trade Commission (FTC) so that they may be reviewed for compliance with the antitrust laws before they are consummated.

The premerger notification mechanism was developed to advise antitrust authorities of proposed mergers involving very large firms and to facilitate enjoining illegal mergers before their consummation. The Senate report found that:

> Presently, the Government can stop few illegal mergers before they take place. Once a merger is consummated, the average case takes 5–6 years to resolve, during which time the acquiring entity retains the illegal profits and other fruits of the transaction. Securing adequate relief after the assets, management, and technology of the two merged firms have been together for that 5–6 year period is virtually impossible. As a result, the original state of competition is rarely restored upon ultimate disposition of the judicial proceeding.

S. Rep. No. 803, 94th Cong., 2d sess. 61 (1976).

Giving the antitrust enforcement agencies the opportunity to review proposed mergers and, if necessary, enjoin their consummation if they would violate the antitrust laws, has helped alleviate the problem of "unscrambling the eggs" once a merger has occurred.

The premerger notification system created by the Hart-Scott-Rodino Antitrust Improvements Act is basically sound. There are several facets of the process that require improvement, however, and S. 431 addresses one of them.

The FTC, in conjunction with the Antitrust Division of the U.S. Department of Justice, has developed a rather complex set of regulations and informal advisory opinions to implement the premerger notification system. It is necessary for the FTC and the Antitrust Division to have the flexibility to apply section 7A, in accordance with its purposes, to the different sets of facts which arise. In general, both agencies have done a good job.

The agencies have failed, however, to solve a glaring problem in the way the Act has been applied to acquisitions by partnerships. Under current agency rules and interpretations, a partnership need not report a proposed acquisition if the partnership itself does not possess assets, in addition to the cash it has on hand to make the acquisition, that meet the monetary thresholds of the Act. Thus, large firms and wealthy individuals may avoid notifying the Government about a proposed merger by forming and underfinanced partnership to make the acquisition.

The attempted takeovers of Phillips Petroleum and Shamrock Oil Co. by T. Bonne Pickens were structured as partnership acquisitions. Likewise, Sir James Goldsmith formed a partnership in his attempted takeover of Goodyear Tire & Rubber Co.

It is unacceptable for this loophole in the premerger notification system to continue to exist. This conclusion was acknowledged by statement received by the Committee concerning S. 431 including those of the U.S. Department of Justice, the FTC, the American

Bar Association, the National Association of Manufacturers, the Business Roundtable, and the U.S. Chamber of Commerce.

While the FTC and the Department of Justice have been aware of the partnership loophole since at least September 1985, the agencies have not promulgated regulations to close it. Notice and comment rulemaking was commenced by the FTC in September 1985, addressing, among other things, the partnership loophole. The proposal to close the partnership loophole contained in that rulemaking was abondoned by the FTC without taking effect.

The FTC took no further public action to close the partnership loophole until after Senators Metzenbaum, DeConcini, and Simon introduced S. 431 on February 2, 1987. Just before the Subcommittee on Antitrust, monopolies, and business rights held a hearing on that bill on February, 26, 1987, the FTC authorized the commencement of notice and comment rulemaking on a second proposed regulation to close the loophole. The period for written comment on the proposed regulation closed on April 6, 1987, more than a year and a half after the first proposal was presented for public comment.

The FTC's proposed regulation, however, would not close the loophole completely. It would still be relatively simple for wealthy individuals or large companies to avoid notifying the Government of a proposed acquisition under the FTC's proposal.

It may not be possible to close the loophole entirely since an enterprising lawyer might be able to get around the requirements of any provision. However, it is important to draw the line around mergers raising antitrust considerations which are consummated through partnerships so that evasion of the premerger notification rules would be neither simple nor inexpensive.

S. 431 accomplishes that task.

II. History of Legislation

S. 431 was introduced by Senators Metzenbaum, Simon, and DeConcini on February 2, 1987. A hearing on the bill was held on February 26, 1987, and an amendment in the nature of a substitute was reported out of the Subcommittee on Antitrust, Monopolies, and Business Rights by voice vote on March 19, 1987. The committee approved an amendment in the nature of a substitute by voice vote on April 29, 1987.

III. Discussion

The premerger notification scheme contained in Section 7A of the Clayton Act requires parties that intend to merge to report their proposed merger to the Department of Justice and the FTC if:

(1) Either the acquiring party or the acquired party is engaged in commerce or an activity affecting commerce;

(2) Either party has annual net sales or total assets of $100 million or more, and the other party has $10 million or more in annual net sales or total assets; and

(3) The acquiring party would hold 15 percent or more of the voting securities or assets of the acquired party, or more than $15 million worth of its voting securities and assets after the acquisition.

Generally, a party to a proposed merger determines whether or not it possesses the necessary assets to meet the threshold requirements of Section 7A by adding its assets to:

(1) The assets of the entity which controls it and

(2) The assets of any entity controlled by the entity which controls it.

Partnerships are treated differently, however. Under current law, FTC regulations and FTC informal staff opinions, a partnership formed for the purpose of making an acquisition would only count its own assets minus the cash equivalent assets it will use to make the acquisition.[1] The assets of the partners themselves are not counted for purposes of making the determination.

This rule enables large companies and wealthy individuals to form partnerships to avoid filing notice of their proposed mergers with Federal antitrust authorities.

Testimony received by the Committee was unanimous in the view that the partnership loophole must be closed. While the Committee is willing to assume that the Department of Justice and the FTC will finalize their proposed regulation, the issue is whether or not the proposed regulation will actually accomplish its stated intention. The Committee has concluded that the proposed regulation does not close the partnership loophole in a satisfactory manner.

The FTC proposed regulation alters the filing requirement for partnerships by requiring that the assets of a partner be included in the assets of the partnership for purposes of Section 7A if the partner has "the right to 50 percent or more of the profits of the entity, or, having the right in the event of disssolution to 50 percent or more of the assets of the entity." This formulation begins to close the loophole, but does not close it completely.

The following illustration shows how easily Section 7A's reporting requirements could still be evaded by a partnership under the proposed regulation. Assume Exxon, Mobil, and Texaco form a partnership with assets of less that $10 million to acquire Socal. Assume further that all three companies have an equal, one-third, interest in the partnership and that all three companies are general partners. Despite the potential antitrust ramifications of this hypothetical deal, no filing would be required under the FTC's proposed regulation because no partner controls 50 percent or more of the assets of the partnership.

The parties to a merger would not have to report the transaction under the proposed regulation, therefore, as long as no partner possesses a 50 percent or greater interest in the partnership. A partnership could avoid reporting a proposed acquisition while still denominating a "controlling partner" by giving the "controlling" partner a 49 percent interest and making it the "general partner."

Such simple evasion of the reporting requirement would not be possible under S. 431. Under S. 431, a partner's assets would be included in the calculation of the partnership's assets if:

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[1] There are two qualifications to this general formula. First, it applies only to the first acquisition of a newly formed partnership. The assets counted if the partnership were to make a second acquisition would include the holdings acquired as a result of the first acquisition. Second, if the partnership has prepared regular financial statements, it must refer to those statements in determining its size under Section 7A.

(1) As in the proposed regulation, it had a 50 percent or greater interest in the partnership or

(2) It were a general partner. To complete the example, the assets of Exxon, Mobil, and Texaco in the illustration above, therefore, would be counted with the partnership's assets under S. 431.

IV. Text of S. 431 as Amended

A BILL To amend the Clayton Act regarding partnerships.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 7A of the Clayton Act is amended by adding at the end thereof the following new subsection:

"(k) For purposes of this section, the annual net sales and total assets of a person shall include, in the case of a partnership, the annual net sales or total assets of any general partner and any partner having the right to 50 per centum or more of the profits of the partnership, or having the right in the event of dissolution to 50 per centum or more of the assets of the partnership."

Sec. 2. This Act and the amendments made by this Act shall become effective sixty days after the date of enactment of this Act.

V. Section-by-Section Analysis

Section 1: Section 1 would amend the Clayton Act to require that the assets and sales of controlling partners and general partners be included in determining the size of a partnership. Thus, for purposes of determining the size of a partnership, the annual net sales and total assets of a partner who qualified as either a general partner or as a partner having a right to 50 percent of the partnership's profits or 50 percent of the partnership's assets upon dissolution would be aggregated with the partnership's assets (minus the cash or cash equivalent assets with which the acquisition would be made). If more than one partner were a controlling or general partner, that partner's assets and net sales would not be aggregated with other such partners. Instead, the assets and sales of each such partner would be separately added to those of the partnership for purposes of determining the size of the partnership.

One factor which the enforcement agencies should use as a guide to determining whether a person is a "general partner" is the definition of a "general partner" under State law. Beyond this, the Committee has decided not to define "general partner." Instead, the U.S. Department of Justice and the FTC may define it further, if necessary, in accordance with Section 7A(d). This will provide the antitrust agencies with flexibility in enforcing the new provision. So, for example, if the agencies find that parties to acquisitions without antitrust significance must report under the new provision, the agencies may exclude those transactions from the reporting requirements of the Act.

The bill does not address who is obligated to notify the Federal enforcement agencies about the proposed merger or the form of notification. The Committee leaves these determinations of, for example, who should file (the partnership, the partner, or both) and how

many filings must be submitted, to the U.S. Department of Justice and the FTC.

The bill is not meant to preclude the Federal enforcement agencies from promulgating regulations under Section 7A(d) which establish additional reporting requirements for partnerships involved in proposed mergers. The bill sets only the minimum standards for premerger reporting by partnerships. The agencies are free to promulgate regulations implementing the bill and further defining terms in the bill, if necessary. In addition, as stated above, the enforcement agencies may determine that partnerships must report proposed mergers in circumstances not covered by the bill and promulgate regulations to that effect.

Section 2: Section 2 provides that the Act becomes effective 60 days after enactment. Thus, the Act applies to all transactions to be consummated 60 days after enactment. Postponing the effective date of this Act for 60 days will provide persons with enough time to conform their plans to the requirements of the Act. With a 60-day compliance period, parties who are in the process of formulating merger plans will be able to take the new Act into account. If, however, the parties will consummate the transaction within 60 days of the date of enactment, they need not comply with these new provisions.

VI. Estimated Cost of Legislation

In accordance with paragraph 11(a) of rule XXVI of the Standing Rules of the Senate and Section 403 of the Congressional Budget Act of 1974, the Committee provides the following cost estimate, prepared by the Congressional Budget Office:

U.S. Congress,
Congessional Budget Office,
Washington, DC, May 4, 1987.

Hon. Joseph R. Biden, Jr.,
Chairman, Committee on the Judiciary,
U.S. Senate, Washington, DC.

Dear Mr. Chairman. The Congressional Budget Office has reviewed S. 431, a bill to amend the Clayton Act regarding partnerships, as ordered reported by the Senate Committee on the Judiciary, April 29, 1987.

Based on information provided by the Department of Justice, CBO estimates that enacting S. 431 would result in no significant cost to the federal government and in no cost to state or local governments. The bill would extend, to cover all partnerships, the laws governing pre-notification of mergers.

If you wish further details on this estimate, we will be pleased to provide them.

With best wishes,
Sincerely,

Edward M. Gramlich,
Acting Director.

VII. Regulatory Impact Statement

Pursuant to paragraph 11(b), rule XXVI of the Standing Rules of the Senate, the Committee has concluded that the Act establishes no new regulatory scheme and, therefore, will have no adverse impact.

VIII. Changes in Existing Law

In compliance with paragraph 12 of the rule XXVI of the Standing Rules of the Senate, changes in existing law made by S. 431, as reported, are shown as follows (new matter is printed in italic, existing law in which no change is proposed is shown in Roman);

UNITED STATES CODE

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TITLE 15—COMMERCE AND TRADE

CHAPTER 1—MONOPOLIES AND COMBINATIONS IN RESTRAINT OF TRADE

* * * * * * *

§ 18a Premerger notification and waiting period

(a) Filing.—Except as exempted pursuant to subsection (c), no person shall acquire, directly or indirectly, any voting securities or assets of any other person, unless both persons (or in the case of a tender offer, the acquiring person) file notification pursuant to rules under subsection (d)(1) and the waiting period described in subsection (b)(1) has expired, if—

(1) the acquiring person, or the person whose voting securities or assets are being acquired, is engaged in commerce or in any activity affecting commerce;

* * * * * * *

(j) Report to Congress; Legislative Recommendations.—Beginning not later than January 1, 1978, the Federal Trade Commission, with the concurrence of the Assistant Attorney General, shall annually report to the Congress on the operation of this section. Such report shall include an assessment of the effects of this section, of the effects, purpose, and need for any rules promulgated pursuant thereto, and any recommendations for revisions of this section.

(k) For purposes of this section, the annual net sales and total assets of a person shall include, in the case of a partnership, the annual net sales or total assets of any general partner and any partner having the right to 50 per centum or more of the profits of the partnership, or having the right in the event of dissolution to 50 per centum or more of the assets of the partnership.

Sec. 2. This Act and the amendments made by this Act shall become effective 60 days after the date of enactment of this Act.

IX. Vote of the Committee

On April 29, 1987, with a quorum present, by voice vote, the Committee on the Judiciary ordered S. 431 as amended favorably reported.

X. Minority Views

MESSRS. THURMOND, HATCH, SIMPSON, AND HUMPHREY ON S. 431

We have indicated, in the Subcommittee markup and elsewhere, that we are opposed to this legislation but not opposed to the purposes behind it. We are not opposed to revising the regulations under the Hart-Scott-Rodino Act's premerger notification program in order to close the so-called "partnership loophole" in those regulations. We oppose this bill, however, because it is unnecessary and overbroad as a means of closing the partnership loophole.

We share the view of the majority of the witnesses who testified on this matter that the loophole should be fixed by regulatory rulemaking procedure. That process is already under way, as the majority knows. With the concurrence of the Department of Justice, the Federal Trade Commission published a proposed rule on partnerships in the Federal Register on March 6. The only thing required for final adoption of the new rule is the expiration of the period of time for public comment under the Administrative Procedures Act. It should be noted, in response to remarks by the majority, that the Federal Trade Commission has been diligently searching for the correct solution to the partnership loophole ever since the reporting problems came to the Commission's attention. Contrary to the suggestion of the majority, the partnership loophole does not reflect a longstanding omission by the Government; rather, the loophole in the regulations has become apparent only from recent experience with the reporting requirements and, since its first experience with the loophole, the Commission has been thoughtfully considering the *appropriate* corrective action. An earlier proposed rule change was pulled back in response to significant critical comments. The fact that the Commission took no "public action" until recently, as the majority puts it, is of no importance, because the work of the antitrust authorities on a proper solution has nevertheless continued unabated. It is our view that the Congress should allow the FTC to complete the regulatory correction of the partnership reporting loophole, and that legislation in this area of regulation would be inappropriate.

Legislation aimed at closing the loophole may be construed as "occupying the field" in an area that Congress has previously left entirely to the FTC for promulgation of appropriate rules. Such legislative revision of rules may stymie or preclude subsequent rulemaking efforts to refine the treatment of aquisitions by partnership. The antitrust agencies may very soon discover unforeseen problems with the premerger reporting scheme, and they should be left the flexibility to fashion appropriate response through additional rulemaking. Such regulatory matters are technical and complex, and the Federal Trade Commission is much better equipped

than the Congress to complete the fine tuning of modifications of the premerger notification program. As mentioned, in the Hart-Scott-Rodino Act, Congress wisely left such regulatory matters to the FTC, which is best prepared to balance the many intricacies and considerations that are involved in such adjustments. Accordingly, we oppose the legislative approach to the regulatory loophole.

The "loophole", of course, is a gap in the FTC's premerger notification regulations that allows partnerships to be formed by persons for the sole purpose of making an acquisition without filing premerger notification reports. There is widespread agreement that this loophole should be closed, so that owners of partnerships will be required to submit the same disclosures as other business enterprises when they propose mergers. The differences of opinion turn on the method of making the adjustment, as described, and the breadth of the remedy.

The FTC's proposed rule would be less inclusive than the bill, S. 431, and is, therefore, a more appropriate and less burdensome response to the problem at hand. The bill provides that for premerger notification purposes, the term "person" shall include, in the case of a partnership, any general partner and any partner with an equity interest of 50 percent or more. The bill would aggregate the size of each such partner with that of the partnership in order to determine the size of the partnership. By contrast, the approach taken by the FTC proposed rule focuses on who ultimately controls each of the parties in a merger or acquisition. Under the current FTC rules and the proposed rule, both the filing obligations of the acquiring and acquired "persons" and the information to be submitted are determined by looking at the "ultimate parent entity" and all entities that it controls. In other words, the FTC's proposed rule focuses on who ultimately controls a partnership.

Extensive study of this issue by the Federal Trade Commission indicates that the potentially significant, unreported transactions—those that currently slip through the loophole—are most likely to be acquisitions by partnerships dominated by one person. Therefore, requiring a report covering that dominant or controlling person should close the loophole effectively. Alternative approaches to closing the loophole, such as that of S. 431, are likely to be overinclusive by requiring filings for competitively insignificant transactions. Including all general partners within the "person of the partnership would appear to turn some currently unreportable leveraged buyouts into reportable acquisitions if they are undertaken by a partnership. These leveraged buyouts typically do not combine businesses and thus lack antitrust significance. Furthermore, a leveraged buyout, if undertaken through a shell corporation, would not be reportable if the corporation is its own "ultimate parent entity" under the rules. For these reasons, the FTC has concluded that no purpose is served by including all general partners in the filing requirement.

Beyond the problem of overinclusiveness in S. 431, there is ambiguity about whether general partners and partners with equity interests of 50 percent or more would have filing obligations separate and apart from those of the partnerships themselves. The bill clearly aggregates the size of each such partner with that of the

partnership in order to determine the size of the partnership. It is not clear whether the bill does or does not require separate filing obligations for such partners as well. We would regard such a separate filing requirement as excessively burdensome. To the extent that the determination of who must file separate premerger notification reports is left to the rulemaking discretion of the Federal Trade Commission, we would urge the Commission not to create separate filing obligations for each general partner or each noncontrolling partner.

In conclusion, we believe that S. 431 is unnecessary, inappropriate and overinclusive legislation. The partnership premerger notification loophole, which we acknowledge to be a problem, is very close to being corrected in a more appropriate way—through the FTC's laudable rulemaking proposal. We join with the Justice Department, the FTC, the American Bar Association Section of Antitrust Law, the business community and even the expert witness at the hearing on the bill in urging Congress to withhold from legislating in this area and to permit the antitrust agencies to complete their on-going regulatory revision.

STROM THURMUND.
ORRIN G. HATCH.
ALAN K. SIMPSON.
GORDON HUMPHREY.

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Calendar No. 208

100TH CONGRESS
1st Session

SENATE

REPORT
100-89

AMENDING THE CLAYTON ACT REGARDING INTERLOCKING DIRECTORATES AND OFFICERS

JUNE 25 (legislative day, JUNE 23), 1987.—Ordered to be printed

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Mr. BYRD (for Mr. BIDEN), from the Committee on the Judiciary, submitted the following

REPORT

[To accompany S. 1068]

The Committee on the Judiciary, to which was referred the bill (S. 1068) to amend section 8 of the Clayton Act (15 U.S.C. Section 19) regarding interlocking directorates and officers, having considered the same, reports favorably thereon with an amendment and recommends that the bill as amended do pass.

CONTENTS

	Page
I. Purpose of S. 1068	1
II. Background of the legislation	2
III. History of S. 1068	3
IV. Text of the bill as reported	3
V. Summary of the bill	4
A. Jurisdictional threshold	4
B. De minimis exceptions	5
C. Application to officers	6
D. Time of application	6
VI. Section-by-section analysis	7
VII. Cost estimate	7
VIII. Regulatory impact statement	8
IX. Changes in existing law	8

I. PURPOSE OF S. 1068

S. 1068 amends section 8 of the Clayton Act, which prohibits "interlocking directors"—the same person sitting on the board of directors of competing corporations. S. 1068 has three basic purposes:

S523-6

(1) it raises the jurisdictional threshold, based on the net worth, for companies covered by the section to reflect our modern economy and inflation;

(2) it creates certain "de minimis" exceptions to coverage of the section in order to avoid application when no potential for competitive harm exists; and

(3) it expands the coverage of the section to include officers elected or chosen by the board of directors of competing corporations in order to prevent potential harm to competition from interlocking officers.

II. Background of the Legislation

Section 8 of the Clayton Act was enacted in 1914. With certain exceptions, it bars the same individual from serving on the board of directors of corporations in competition with one another. This provision was enacted as part of the broad antitrust reforms advocated by President Woodrow Wilson and adopted by Congress in the Clayton Act to supplement the provisions of the 1890 Sherman Act. President Wilson argued that interlocking directorates were a device which concentrated economic power at the expense of the public, and the legislative history of Section 8 reflects that concern. As the Court of Appeals for the Ninth Circuit has stated:

> . . . the legislative materials establish that the Clayton Act was intended to supplement and strengthen the Sherman Act in preserving a free competitive economy; that interlocking directorates were regarded as a precursor to restraint and monopoly and thus as a most serious threat to free competition; and that such interlocking directorates were strongly condemned. (*U.S.* v. *Crocker Nat. Corp.*, 656 F.2d 428 (1981)).

While the fundamental purpose of Section 8 is still valid more than 70 years after its enactment, a number of proposals have been made in recent years to reform this section to make it more consistent with modern economic and competitive considerations. During the 99th and 100th Congress, a number of proposals were made to amend Section 8. For example, the Administration submitted a proposal in the 99th Congress, introduced by Senator Thurmond as S. 2163, and an identical proposal again in the 100th Congress, introduced by Senator Thurmond as a part of S. 635. Senator Metzenbaum, joined by Senator Thurmond, also introduced S. 1068 in the 100th Congress.

All of these proposals sought to retain the basic ban on individuals serving on boards of competing corporations. However, they also recognized a need for Congress to reconsider the class of corporations covered by the section and whether there should be exceptions for competitively insignificant overlaps. The absence of a realistic de minimis exception for very small competitive overlaps has discouraged qualified persons from serving as directors when no potential for competitive harm exists.

During the 99th Congress, the Committee on the Judiciary held a hearing regarding proposals to modify Section 8. (See "The Interlocking Directorate Act of 1986," Hearing of the Senate Committee

on the Judiciary on S. 2163, 99th Cong., 2d sess; April 28, 1986.) Several individuals and groups testified in favor of modifying Section 8, including the Assistant Attorney General, Antitrust Division, Department of Justice; the American Bar Association; the U.S. Chamber of Commerce; the Association of the Bar of the City of New York; the Business Roundtable, and others.

III. History of S. 1068

Early in the 100th Congress, Senator Metzenbaum, Senator Thurmond, the Department of Justice and other interested persons engaged in extensive discussions regarding possible approaches to the revision of Section 8 prior to the introduction of legislation. As a result of these discussions, S. 1068 was introduced on April 22, 1987, as a bipartisan measure by Senator Metzenbaum and Senator Thurmond. The bill was referred to the Subcommittee on Antitrust, Monopolies and Business Rights of the Committee on the Judiciary. Because there was a broad consensus as to the approach reflected in S. 1068, the Committee did not believe additional hearings were necessary during the 100th Congress.

S. 1068 was reported favorably by poll from the subcommittee on April 29, 1987, by a vote of 8–0 (Senator Simon not voting). It was reported favorably by voice vote from the full Committee on May 19, 1987.

IV. Text of the Bill as Reported

A BILL To amend the Clayton Act regarding interlocking directorates and officers

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 8 of the Clayton Act is amended to read as follows:

"Sec. 8. (a)(1) No person at the same time shall be a director or officer of any two corporations, each of which has capital, surplus and undivided profits aggregating more than $10,000,000, as adjusted pursuant to this subsection, engaged in whole or in part in commerce, other than banks, banking associations, trust companies, and common carriers subject to subtitle IV of title 49, United States Code, if such corporations are by virtue of their business and location of operation, competitors so that the elimination of competition by agreement between them would constitute a violation of any of the provisions of any of the antitrust laws.

"(2) Notwithstanding the provisions of paragraph (1), simultaneous service as a director or officer of two corporations shall not be prohibited by this section if (A) the aggregate competitive sales of either corporation are less than $1,000,000, as adjusted pursuant to this subsection, (B) the aggregate competitive sales of either corporation are less than 1 percent of that corporation's total sales, or (C) the aggregate competitive sales of each corporation are less than 4 percent of that corporation's total sales. For purposes of this paragraph, 'aggregate competitive sales' means the aggregate gross revenues for all products and services sold by one corporation in competition with the other, determined on the basis of annual gross revenues for such products and services over the last completed fiscal year. For purposes of this section, 'total sales' means the

aggregate gross revenues for all products and services sold by one corporation over the last completed fiscal year.

"(3) The eligibility of a director or officer under the provisions of paragraph (1) shall be determined by the capital, surplus and undivided profits of each corporation at the end of that corporation's last completed fiscal year.

"(4) For purposes of this section, the term 'officer' means an officer elected or chosen by the Board of Directors.

"(5) For each fiscal year commencing after September 30, 1987, the $10,000,000 and $1,000,000 thresholds in this section shall be increased (or decreased) as of October 1 each year by an amount equal to the percentage increase (or decrease) in the Gross National Product, as published by the Department of Commerce or its successor, for the year then ended, over or under the level so established for the year ending September 30, 1986. At the beginning of October of each year, the Federal Trade Commission shall publish the adjusted amounts required by this paragraph.

"(b) When any persons elected or chosen as a director or officer of any corporation subject to the provisions of this Act is eligible at the time of his election or selection to act for such corporation in such capacity, his elibility to act in such capacity shall not be affected and he shall not become or be deemed amenable to any of the provisions hereof by reason of any change in the capital, surplus and undivided profits, or affairs of such corporation from whatsoever cause, whether specifically excepted by any of the provisions hereof or not, until the expiration of one year from the date on which an event causing ineligibility occured, or, if practical, the next regularly scheduled election of directors, whichever occurs first.".

V. Summary of the Bill

S. 1068 amends Section 8 of the Clayton Act is three ways:

(1) it increases that jurisdictional threshold for application of the section to corporations from $1 million in net worth to $10 million in net worth;

(2) it creates three "de minimis" exceptions to applications of the section in cases of insignificant competitive overlaps; and

(3) it expands the section to cover offices elected or chosen by the board of directors. Each of these revisions is discussed in more detail below.

A. JURISDICTIONAL THRESHOLD

Section 8 applies to corporations, "any one of which has capital, surplus, and undivided profits aggregating more than $1,000,000 . . ." This phrase, meaning net worth, was included in the original statute enacted in 1914. Because of the substantial increase in price levels since 1914, this dollar threshold is obviously far lower than the size of corporations Congress originally sought to cover. Sections (a)(1) of the bill increases this threshold to $10 million. By increasing the threshold, it is the intention of the Committee to maintain the original congressional intent of applying the sections only to corporations which are engaged in some significant degree of commerce.

In addition to raising the threshold, S. 1068 provides in section 8(a)(5) for an annual adjustment in the jurisdictional threshold, based on the gross national product. This provision insures that the threshold provided in the bill will be regularly modified to maintain at a realistic level the minimum net worth required for application of this section to the nation's corporations.

B. DE MINIMIS EXCEPTIONS

Section 8(a)(2) of S. 1068 creates three separate de minimis exceptions to the applications of the section. The intent of the Committee is to preclude from the prohibition against interlocking directors competitive overlaps which are too small to have competitive significance in the vast majority of situations. The courts have held that the current section applies to common director situations, even if the overlap is insignificant. (See, e.g., *TRW* v. *Federal Trade Commission*, 647 F.2d 942, 948 (9th Cir. 1981); *In re Borg-Warner Corp.*, 3 Trade Reg. Rep. (CCH) para. 22,049 (F.T.C. June 23, 1983) rev'd on other grounds, 746 F. 2d 108 (2d. Cir. 1984).

The bill provides a de minimis exception in three situations:

(1) the aggregate competitive sales of either corporation are less than $1 million;

(2) the aggregate competitive sales of either corporation are less than 1 percent of that corporation's total sales; and

(3) the aggregate competitive sales of each corporation are less than 4 percent of total sales of that corporation. If any of these three exceptions apply, the prohibition of the section would not be triggered.

In calculating whether any of these de minimis safe harbors apply, corporations subject to the act would be required to aggregate all products and services in competition with another corporation for comparison with total sales. In a case where a single corporate entity is involved, total sales will be based on total corporate sales.

When the common director or officer serves a parent corporation and the competitive overlap involves subsidiary corporations, the question arises as to when the sales of the subsidiary are attributed to the parent in order to determine when the parent corporations will be held to be competitors. It is not the intention of the Committee to address the way in which the courts have determined when sales of subsidiary corporations are to be attributed to the parent. In the event that the subsidiary's sales are attributed to the parent, "total corporate sales" of the parent should include sales of the parent as well as sales of all subsidiaries for which sales should be so attributed. In a case where a common director or officer serves only a subsidiary corporation, "total corporate sales" should include only the sales of the affected subsidiary since the subsidiaries' boards are presumed to control only the actions of the subsidiaries.

It is not the intention of the Committee to alter the way in which the courts have determined whether products or services sold by one corporation are in competition with products or services sold by another corporation. The courts have looked to a wide variety of factors to determine whether competition exists. (See,

e.g., *TRW* v. *Federal Trade Commission, supra; Protectoseal Co.* v. *Barancik*, 484 F.2d 585 (7th Cir. 1973)). Similarly, it is not the intention of the Committee to alter the principle that a violation of Section 8 does not require a showing of harm to competition but rather is a "per se" violation. (*Protectoseal Co.* v. *Baroncik, supra; U.S.* v. *Sears, Roebuck & Co.*, 111 F. Supp. 614 (S.D.N.Y. 1953).

The Committee has determined not to modify the phrase in Section 8 applying the section to "competitors, so that the elimination of competition by agreement between them would constitute a violation of any of the provisions of any of the antitrust laws." It has been argued that this language restricts the application of the bar on common directors only to corporations which would violate Section 7 by merging. However, this argument has been rejected and the courts have held this language was intended only to mean that the corporations are competitors. (See, *U.S.* v. *Sears, Roebuck & Co., supra.*)

C. APPLICATION TO OFFICERS

Section 8(a)(1) of S. 1068 expands the current ban on interlocking directors to include officers. "Officers" are defined to mean officers "elected or chosen by the Board of Directors." The Committee believes that there is an equal or perhaps greater potential for competitive harm from persons serving as officers of competitor corporations. Consequently, this expansion of the coverage of the section is warranted to bar persons from serving simultaneously as an officer of competing corporations or as an officer of one corporation and a director of a competing corporation.

D. TIME OF APPLICATION

S. 1068 contains a number of provisions intended to make clear how the standards contained in the bill are to be determined and when the prohibitions on common directors or officers are triggered. Section (a)(2) provides that "aggregate competitive sales" and "total sales" are to be determined based on sales for the last completed fiscal year. Similarly, capital, surplus and undivided profits—or net worth—is to be determined based on the net worth of the corporation at the end of the last fiscal year.

Since 1914, Section 8 has provided a limited grace period in the case where a change in circumstances results in what would otherwise constitute a violation by a sitting director. S. 1068 clarifies the circumstances under which this grace period applies. In a case where a change in the net worth or other affairs of a corporation (e.g., the introduction of a new product line) results in a competitive overlap, there is no violation for 1 year from the change which triggered application of the section, or until the next regularly scheduled board of directors election, whichever occurs first.

This subsection provides an exception if the regularly scheduled election is so soon than it is impractical to elect a new director in that election. For example, if the event causing the statute to apply occurs on January 1, and the next regularly scheduled election is January 15, it may be impractical for the corporation to select a new officer or director at that election. In that case, the officer or director should be replaced at the next regularly scheduled elec-

tion, or in any event, within 1 year. In a case where the application of the grace period is unclear, resignation by the affected officer or director prior to selection of his or her replacement would insure that the corporation does not violate Section 8.

VI. Section-by-Section Analysis

S. 1068 strikes the existing language of Section 8 and substitutes a new text. The bill eliminates the first three paragraphs of Section 8 which initially applied to banks and related institutions. These provisions have been superseded by more specific provisions applicable to financial institutions. These include the Depository Institution Management Interlocks Act, 12 U.S.C., Sections 3201, et seq., and Section 10(c) of the Investment Company Act, 15 U.S.C, Section 80a–10c. Other specific provisions in existing law cover other industries.

The amended Section 8(a)(1) adds officers to the current prohibition and raises the jurisdictional threshold for application of Section 8 to $10 million in capital, surplus and undivided profits.

Section 8(a)(2) provides for three de minimis exceptions to coverage of the section. It also provides that aggregate competitive sales are to be based on annual gross revenues for the last completed fiscal year and that total sales means the aggregate gross revenues for all products and services.

Section 8(a)(3) provides that the jurisdictional threshold determination shall be based on capital, surplus and undivided profits (or net worth) at the end of the last completed fiscal year.

Section 8(a)(4) defines officers to mean officers elected or chosen by the board of directors.

Section 8(a)(5) provides that the $10 million jurisdictional threshold is to be increased each year in conformity with the gross national product.

Section 8(b) provides for a grace period after a change in affairs which would make a sitting director or officer otherwise ineligible to serve. No violation would occur for 1 year after the event causing ineligibility or, if practical, the next regularly scheduled election, whichever is earlier.

VII. Cost Estimate

U.S. Congress,
Congressional Budget Office,
Washington, DC, May 27, 1987.

Hon. Joseph R. Biden, Jr.
Chairman, Committee on the Judiciary,
U.S. Senate, Washington, DC.

Dear Mr. Chairman: The Congressional Budget Office has reviewed S. 1068, a bill to amend the Clayton Act regarding interlocking directorates and officers, as ordered reported by the Senate Committee on the Judiciary, May 19, 1987.

CBO estimates that enacting this bill would result in no significant costs to the federal government. The bill would allow an individual to serve as a director or officer for two competing corporations whose competitive sales are small or whose net worth is $10

million or less. The bill would also extend existing restrictions on interlocking directors to officers. Based on information provided by the Department of Justice, we expect that this bill would not necessitate any significant additional enforcement costs for the federal government.

Enacting this bill would not affect the budgets of state or local governments.

If you wish further details on this estimate, we will be pleased to provide them.

With best wishes,

Sincerely,

EDWARD M. GRAMLICH,
Acting Director.

VIII. REGULATORY IMPACT STATEMENT

In compliance with paragraph 11(b), rule XXVI of the Standing Rules of the Senate, the Committee, after due consideration, concluded that this bill will not have any regulatory impact.

IX. CHANGES IN EXISTING LAW

In compliance with paragraph 12 of rule XXVI of the Standing Rules of the Senate, changes in existing laws proposed to be made by S. 1068 are shown as follows: existing law to be omitted is enclosed in black brackets, new matter is printed in italic and existing law in which no change is proposed is shown in roman.

UNITED STATES CODE

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TITLE 15—COMMERCE AND TRADE

CHAPTER 1—MONOPOLIES AND COMBINATIONS IN RESTRAINT OF TRADE

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§ 19. Interlocking directorates and officers.

[No private banker or director, officer, or employee of any member bank of the Federal Reserve System or any branch thereof shall be at the same time a director, officer, or employee of any bank, banking association, savings bank, or trust company organized under the National Bank Act [see 12 USCS § 38] or organized under the laws of any State or of the District of Columbia, or any branch thereof, except that the Board of Governors of the Federal Reserve System may by regulation permit such service as a director, officer, or employee of not more than one other such institution or branch thereof; but the foregoing prohibition shall not apply in the case of any one or more of the following or any branch thereof:

[(1) A bank, banking association, savings bank, or trust company, more than 90 per centum of the stock of which is owned

directly or indirectly by the United States or by any corporation of which the United States directly or indirectly owns more than 90 per centum of the stock.

[(2) A bank, banking association, savings bank, or trust company which has been placed formally in liquidation or which is in the hands of a receiver, conservator, or other official exercising similar functions.

[(3) A corporation, principally engaged in international or foreign banking or banking in a dependency or insular possession of the United States which has entered into an agreement with the Board of Governors of the Federal Reserve System pursuant to section 25 of the Federal Reserve Act [12 USCS §§ 601-604A].

[(4) A bank, banking association, savings bank, or trust company, more than 50 per centum of the common stock of which is owned directly or indirectly by persons who own directly or indirectly more than 50 per centum of the common stock of such member bank.

[(5) A bank, banking association, savings bank, or trust company not located and having no branch in the same city, town, or village as that in which such member bank or any branch thereof is located, or in any city, town or village contiguous or adjacent thereto.

[(6) A bank, banking association, savings bank, or trust company not engaged in a class or classes of business in which such member bank is engaged.

[(7) A mutual savings bank having no capital stock.

[Until February 1, 1939, nothing in this section shall prohibit any director, officer, or employee of any member bank of the Federal Reserve System, or any branch thereof, who is lawfully serving at the same time as a private banker or as a director, officer, or employee of any other bank, banking association, savings bank, or trust company, or any branch thereof, on the date of enactment of the Banking Act of 1935 [Aug. 23, 1935], from continuing such service.

[The Board of Governors of the Federal Reserve System is authorized and directed to enforce compliance with this section, and to prescribe such rules and regulations as it deems necessary for that purpose.

[From and after two years from the date of the approval of this Act [Oct. 15, 1914] no person at the same time shall be a director in any two or more corporations, any one of which has capital, surplus, and undivided profits aggregating more than $1,000,000, engaged in whole or in part in commerce, other than banks, banking associations, trust companies, and common carriers subject to the Act to regulate commerce, approved February fourth, eighteen hundred and eighty-seven [49 USCS §§ 1 et seq.], if such corporations are or shall have been theretofore, by virtue of their business and location of operation, competitors, so that the elimination of competition by agreement between them would constitute a violation of any of the provisions of any of the antitrust laws. The eligibility of a director under the foregoing provision shall be determined by the aggregate amount of the capital, surplus, and undivided profits, exclusive of dividends declared but not paid to stockholders, at the

end of the fiscal year of said corporation next preceding the election of directors, and when a director has been elected in accordance with the provisions of this Act [15 USCS §§ 12 et seq.; 29 USCS §§ 52 et seq.] it shall be lawful for him to continue as such for one year thereafter.

[When any person elected or chosen as a director or officer or selected as an employee of any bank or other corporation subject to the provisions of this Act [15 USCS §§ 12 et seq.; 29 USCS §§ 52 et seq.] is eligible at the time of his election or selection to act for such bank or other corporation in such capacity, his eligibility to act in such capacity shall not be affected and he shall not become or be deemed amenable to any of the provisions hereof by reason of any change in the affairs of such bank or other corporation from whatsoever cause, whether specifically excepted by any of the provisions hereof or not, until the expiration of one year from the date of his election or employment.]

SEC. 8. (a)(1) No person at the same time shall be a director or officer of any two corporations, each of which has capital, surplus and undivided profits aggregating more than $10,000,00, as adjusted pursuant to this subsection, engaged in whole or in part in commerce, other than banks, banking associations, trust companies, and common carriers subject to subtitle IV of title 49, United States Code, if such corporations are by virtue of their business and location of operation, competitors so that the elimination of competition by agreement between them would constitute a violation of any of the provisions of any of the antitrust laws.

(2) Notwithstanding the provisions of paragraph (1), simultaneous service as a director or officer of two corporations shall not be prohibited by this section if (A) the aggregate competitive sales of either corporation are less than $1,000,000, as adjusted pursuant to this subsection, (B) the aggregate competitive sales of either corporation are less than 1 percent of that corporation's total sales, of (C) the aggregate competitive sales of each corporation are less than 4 percent of that corporation's total sales. For purposes of this paragraph, "aggregate competitive sales" means the aggregate gross revenues for all products and services sold by one corporation in competition with the other, determined on the basis of annual gross revenues for such products and services over the last completed fiscal year. For purposes of this section, "total sales" means the aggregate gross revenues for all products and services sold by one corporation over the last completed fiscal year.

(3) The eligibility of a director or officer under the provisions of paragraph (1) shall be determined by the capital, surplus and undivided profits of each corporation at the end of that corporation's last completed fiscal year.

(4) For purposes of this section, the term "officer" means an officer elected or chosen by the Board of Directors.

(5) For each fiscal year commencing after September 30, 1987, the $10,000,000 and $1,000,000 thresholds in this section shall be increased (or decreased) as of October 1 each year by an amount equal to the percentage increase (or decrease) in the Gross National Product, as published by the Department of Commerce or its successor, for the year then ended, over or under the level so established for the year ending September 30, 1986. At the beginning of October of

each year, the Federal Trade Commission shall publish the adjusted amounts required by this paragraph.

(b) When any person elected or chosen as a director or officer of any corporation subject to the provisions of this Act is eligible at the time of his election or selection to act for such corporation in such capacity, his eligibility to act in such capacity shall not be affected and he shall not become or be deemed amenable to any of the provisions hereof by reason of any change in the capital, surplus and undivided profits, or affairs of such corporation from whatsoever cause, whether specifically excepted by any of the provisions hereof or not, until the expiration of one year from the date on which an event causing ineligibility occurred, or, if practical, the next regularly scheduled election of directors, whichever occurs first.

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